



Department of Revenue

About DOR

[Home](#) > [Businesses](#) > [Help & Resources](#) > [Legal Library](#) > [Letter Rulings](#) > [LR 17-3: Net Worth Calculation.....](#)

Letter Ruling 17-3: Net Worth Calculation Where Subsidiaries Owned Indirectly Through a Pass-Through Entity

October 23, 2017

I. Introduction

We have received the Letter Ruling request submitted on behalf of your client, in which you ask whether a corporation may, when calculating its net worth pursuant to G.L. c. 63, § 30.8 for purposes of the Massachusetts corporate excise, subtract from the book value of its total assets the book value of its investments in subsidiary corporations held indirectly through a limited liability company.

II. Facts

You state the relevant facts as follows: Parent, a Delaware corporation, owns 100 percent of the voting rights of, and possesses a 92.16 percent membership interest in, LLC, a Delaware limited liability company treated as a partnership for federal income tax purposes. Neither Parent nor LLC currently file in or are subject to tax in Massachusetts.^[1]

LLC owns 100 percent of Sub 1, a Delaware corporation. Sub 1 owns 100 percent of Sub 2, a limited liability company organized in Delaware that has elected to be treated as a corporation for federal income tax purposes. Sub 1 and Sub 2 both currently file in Massachusetts as part of a Massachusetts combined group. See G.L. c. 63, § 32B.

III. Issue

Whether Parent may, in calculating its net worth pursuant to G.L. c. 63, § 30.8 for purposes of the Massachusetts corporate excise, subtract from the book value of its total assets the book value of its investments in Sub 1 and Sub 2, as owned through its ownership of the pass-through entity, LLC.

IV. Ruling

For the reasons discussed below, based on the organizational structure as described, Parent may not subtract from the book value of its total assets the book value of its investments in Sub 1 and Sub 2.

V. Discussion

Corporations doing business in the Commonwealth are subject to the Massachusetts corporate excise. G.L. c. 63, § 39. The Massachusetts corporate excise is calculated by adding two different measures of tax: a net income measure, and either a property measure or a net worth measure, depending on whether the business corporation is a tangible or an intangible property corporation. *Id.*

In this case, in addition to the income measure, Parent would be subject to the net worth measure as set forth in G.L. c. 63, § 30.8. That section provides that to calculate a business corporation's net worth,

the book value of its total assets on the last day of the taxable year shall be reduced by the sum of (1) its liabilities on said date, (2) the book value of its tangible property situated in the commonwealth on said date and subject to local taxation, less the interest of any mortgagee therein, and (3) *the book value on said date of its investment in subsidiary business corporations which represent 80 per cent or more of the voting stock of said subsidiary business corporations or, in the case of a subsidiary business corporation which does not have voting stock, the book value of its investment in such business corporation which represents 80 per cent or more ownership interest.*

G.L. c. 63, § 30.8 (emphasis added). A business corporation's net worth is reduced by the book value of investments in "subsidiary business corporations," but not investments in other entities. See Technical Information Release ("TIR") 14-11, III A. Because LLC is taxed as a partnership and has not elected to be treated as a corporation for tax purposes, LLC is not a business corporation and therefore Parent's investments in LLC cannot be subtracted from the book value of Parent's total assets in calculating Parent's net worth.

In addition, there is no look-through or constructive ownership principle that would apply to treat Parent as owning its proportionate share of LLC's investments. For federal income tax purposes, it is often the case that a partner in a partnership is treated as owning its proportionate share of the partnership's underlying assets (the so-called "aggregate" theory of partnerships).^[2] While an aggregate approach makes sense in the context of an income tax, it has no necessary application in the context of an excise based on the book value of an entity's assets. Furthermore, federal constructive ownership rules, which in certain enumerated circumstances attribute to a partner in a partnership stock owned directly by the partnership,^[3] do not apply for Massachusetts tax purposes unless specifically adopted (see, e.g., Directives 98-1 and 98-2), and they have not been adopted for purposes of the net worth measure. Treating Parent's interest in LLC as a separate property interest rather than an interest in the underlying assets of LLC also comports with the Department's analysis in TIR 99-22. See TIR 99-22, II.B.6 (stating that a parent corporation can reduce its book value by the book value of investments only where it holds its 80 percent interest directly).^[4]

Moreover, as a general matter, tax statutes that confer a tax benefit such as a deduction or exemption are strictly construed.^[5] As several courts have noted, "taxation is the general rule... A taxpayer is not entitled to an exemption unless he shows that he comes within either the express words or the necessary implication of some statute conferring this privilege upon him."^[6] This caution is implicated on these facts because G.L. c. 63, § 30.8 does not expressly or necessarily authorize a parent corporation to subtract the value of its investment (1) in an entity that is not a business corporation or (2) in a business corporation that the parent does not directly own.

Based on the analysis above, Parent may not subtract from the book value of its total assets the book value of its investments in either Sub 1 or in Sub 2 in calculating its net worth for purposes of the corporate excise.

Very truly yours,

/s/Christopher C. Harding

Christopher C. Harding
Commissioner of Revenue

CCH:RHF:db

LR 17-3

^[1] Parent expects to have nexus in Massachusetts and begin filing corporate excise returns in the future.

^[2] See, e.g., Rev. Rul. 99-57, 1999-2 C.B. 678 (applying aggregate principles to hold that a corporate partner which contributed its own stock to a partnership that subsequently sold such stock does not recognize gain on the stock pursuant to IRC § 1032); Rev. Rul. 90-112, 1990-2 C.B. 186 (holding under the aggregate approach that a foreign corporate partner held real property owned by a partnership for the purposes of IRC § 956).

^[3] See, e.g., IRC §§ 267, 318

^[4] TIR 99-22 pertained to the effect of inter-company payments between a parent and subsidiary business corporation on the value of the parent's investments in the subsidiary.

^[5] See, e.g., *Macy's East, Inc. v. Commissioner of Revenue*, 441 Mass. 797, 804 (2004) (holding that surviving corporation could not deduct the pre-merger net operating losses of predecessor entities as the statute defining "net operating loss" did not plainly authorize the deduction in that circumstance).

^[6] See *Animal Rescue League of Boston v. Assessors of Bourne*, 310 Mass. 330, 332 (1941) (holding that the exemption from real property taxation for real property owned by a charitable organization did not apply to real property held in trust by a charitable trustee); *Milton Hospital & Convalescent Home v. Board of Assessors*, 360 Mass. 63, 67 (1971) (relying on this general principle to hold that hospital wing leased as private offices for physicians did not fall within the scope of the real property taxation exemption for property owned by charitable organizations); *South Boston Savings Bank v. Commissioner of Revenue*, 418 Mass. 695, 698 (1994) (finding that a corporate taxpayer's investments in "pass-through" and "participation" certifications fell within the plain and ordinary meaning of then G.L. c. 63, § 11 and therefore could be deducted when computing the former bank excise).

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